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Supreme Court of the United States

October Term—1942.

No. 542

ADDISON S. PRATT, as Trustee of JACELLEN REALTY CORPORATION, Debtor,
Petitioner, (Plaintiff below),

AGAINST

CHEMICAL BANK & TRUST COMPANY and THE CONTINENTAL BANK AND TRUST COMPANY OF NEW YORK,
Respondents, (Defendants below).

BRIEF FOR RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

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Petitioner, (Plaintiff below),

AGAINST

CHEMICAL BANK & TRUST COMPANY and THE CONTINENTAL BANK AND TRUST COMPANY OF NEW YORK,
Respondents, (Defendants below).

Brief for Respondents, in Opposition to Petition for Writ of Certiorari to Review the Judgment of the United States Circuit Court of Appeals for the Second Circuit.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States.

Chemical Bank & Trust Company and The Continental Bank and Trust Company of New York, respondents, respectfully pray that the petition for the issuance for a write of certiorari to review the judgment of the United States Circuit Court of Appeals for the Second Circuit be denied, for the reason that no error was made by the

District Court or by the Circuit Court of Appeals for the Second Circuit in their unanimous affirmance of the judgment of the District Court; for the reason that no question of general public interest is involved; for the reason that the determination does not have any unusual significance or importance in the administration of the bankruptcy act; for the reason that the decision of the Circuit Court of Appeals and the District Court is in conformity with the adjudicated cases of this Court and does not present any novel question of law and involves no interpretation of any Federal Statute, nor does the judgment in the within captioned matter in any manner conflict with the adjudications in this Court or the Courts of the State of New York on the interpretations given to Section 15 of the New York Stock Corporation Law. No statutes affecting the war effort are involved.

Opinions Below.

The opinion of the District Court dismissing the complaint on the merits after a trial, has not been officially reported. The opinion of the Circuit Court of Appeals reported in 129 Fed. (2d) 1016 unanimously affirmed the judgment of the District Court.

Statement of Matter Involved.

The proceedings for the reorganization of the Jacellen Realty Corporation under Section 77B of the Bankruptcy Act were filed for the purposes of promulgating a plan which would contemplate an extension of a first mortgage on the property owned by the corporation and provide for a reduction in the rate of interest payable. The Debtor was unable to obtain the necessary consents to the Debtor's Plan of Reorganization, resulting in the Realty Associates promulgating its Creditor Plan and acquiring the real property, having a substantial value in excess of the first mortgage and all other obligations of the Debtor.

Notwithstanding that all creditors, except the respondent banks, were paid in full, the within action was instituted. The Trustee relied upon an alleged violation of Section 15 of the New York Stock Corporation Law. The evidence however established that *not one* of the six necessary essentials to establish a cause of action under Section 15 of the Stock Corporation Law existed. The District Court held that the Debtor was not insolvent or imminently insolvent in October, 1937, and had not refused to pay its obligations in the regular course of business. The Circuit Court of Appeals affirmed the conclusions reached by the District Judge and further found that the contract between the Debtor and the respondents accomplished, and was equivalent to, an assignment of rents. The money retained by the banks in October, 1937, was not property of the Debtor but the bank's collateral.

Facts.

The Jacellen Realty Corporation, the Debtor, did not engage in general commercial business. The corporation was formed to own and operate one building in the City of New York. Its sole asset was the real property and the rents derived therefrom. Its sole liabilities were the operating charges and the cost of the building construction.

The construction of the building had been completed in 1932 but in 1934 there still remained approximately $175,000 due to sub-contractors. To secure this indebtedness, the rents of the property had been assigned to the sub-contractors. In March, 1934, the contractors offered to take $55,000 in discharge of their $175,000 indebtedness and offered to release their assignment of rents as part of the transaction. The Debtor was unable to pay interest on its first mortgage, and taxes on its real property due to its pledge of the rents to the contractors. An ap-

plication was made to the respondent banks, for a loan in the sum of $54,000 to complete the purchase. The respondents were willing to lend the money *but only on the basis of full and complete security being given to them. They required and received in March, 1934, a pledge of all of the rents and income of the real property as collateral.* They required the designation of their agent to collect the rents and deliver same to them. The respondents then held the rents (for bookkeeping purposes) in an account in the Debtor's name, but subject solely to the control of the respective respondents. The loans were evidenced by collateral demand notes containing the usual provisions giving the respondents liens on all cash or funds in the banks' possession. By the laws of the State of New York, said contract and transaction constituted an equitable assignment of the rents. Section 223, New York Real Property Law: *Sullivan* v. *Rosson,* 223 N. Y. 217; *Van Rennsalaer* v. *Dennison,* 35 N. Y. 393; *Williams* v. *Ingersoll,* 89 N. Y. 508; *Lynch* v. *Conger,* 168 N. Y. S. 856; *Holmes* v. *Evans,* 192 N. Y. 140; *Fairbanks* v. *Sargent,* 117 N. Y. 329; *Crosby* v. *Packer,* 22 F. (2) 611; *Mills* v. *Virginia Carolina Lumber Co.,* 164 F. 168; *Scott* v. *Armstrong,* 146 U. S. 499.

Thus Section 15 of the Stock Corporation Law Act, has no application.

Respondents' Contention.

It is the position of the respondents, that the moneys credited to the loans in October, 1937, were not free funds of Jacellen Realty Corporation, but the Banks' collateral pledged concurrently with the making of the loan. Nothing was transferred from the Debtor in October, 1937, within the purview of Section 15 of the Stock Corporation Law. None of the essentials for a cause of action under Section 15 existed. Jacellen was not insolvent in October,

1937, nor imminently insolvent, but on the contrary, had an equity in its real property in excess of three hundred thousand ($300,000) dollars. Jacellen had no general creditors, in October, 1937, other than the respondents. The corporation conducted its business in the usual course in October, 1937, and paid its obligations when due. The capital stock of Jacellen Realty Corporation was not owned by the respondents, but was merely escrowed or pledged to assure compliance with the contract made in March, 1934, between the respondents and the corporation. The respondents were not preferred, but on the contrary, all creditors except the respondents, received payment in full, and there is still an unpaid balance of indebtedness to them of upwards of $32,000.

The Proof Did Not Support the Plaintiff-Appellant's Cause of Action.

The complaint is based upon a violation of Section 15 of the Stock Corporation Law. Six necessary elements must exist for a recovery by the plaintiff. If any one is lacking, the cause of action must fall. The proof conclusively established that *none* of the essentials existed. The six essentials under Section 15 are as follows:

1. Insolvency or imminent insolvency of the Bankrupt (Debtor).
2. A transfer while insolvent.
3. That the Transferee knew or had reasonable cause to believe that a preference would result.
4. That the Bankrupt (Debtor) intended to give a preference.
5. That there were creditors preferred against by the giving of the transfer.

6. That Debtor-owned property was transferred in October, 1937.

Debtor Was Not Insolvent or Imminently Insolvent in October, 1937.

The uncontradicted testimony established that on the date of the alleged transfer, the corporation had assets in excess of $2,037,827.65 with maximum liabilities not in excess of $1,650,000 (fols. 223-4). The corporation made a profit in every year of its operations (fols. 448-49). It had made principal payments from profits in excess of $105,000.00. The Debtor's profits in 1936 were greater than 1935 and likewise in 1937 its profits were greater than in 1936. Its profits in 1938 in *receivership* were greater than in 1937 (fols. 229-30, 451).

The Debtor Transferred No Property in October, 1937, Intended and Created No Preference; the Respondents Had No Cause to Believe a Preference Could Exist.

The lack of these essentials is adequately discussed in the opinions of both the District Judge and of Judge Clark for the Circuit Court. An equitable assignment resulted in 1934 when the contract was made (cases *supra*). No title passed from the Debtor in 1937 to the funds received by the bank directly from the rents pledged. *Merriam* v. *Wimpheimer,* 25 Fed. Sup. 405; *Irving Trust Company* v. *Metro Goldwyn Mayer,* 246 A. D. 1; *Todarelli* v. *Visigraph,* 34 Fed. (Sup.) 762.

No Aggrieved Creditors.

Neither the District Court nor the Circuit Court, found it necessary to ascertain whether or not there were any aggrieved creditors. Actually there were no aggrieved

creditors. The agreed facts (fol. 991) established that the only possible creditors of the Debtor were as follows:

1. Aeson Corporation
2. General creditors (current bills)
3. Certificate holders (first mortgage issue)
4. Realty Associates (Junior participation in first mortgage)
5. The respondent banks.

Aeson's claim was subordinated to the banks' and was treated as part of the banks' claim (fol. 208). General creditors were fully paid and discharged before the filing of the petition by the Debtor (fols. 221-25). Certificate holders received new certificates for the full amount of their claim together with interest at 5%. The certificate holders were fully secured creditors and not entitled to share in the general assets. Section 57 h, U. S. Bankruptcy Act. Realty Associates received the equity in the property and retained their Junior interest as a second mortgage (fol. 879). Realty Associates was a secured creditor in the full amount of its claim. The fair value of the property, acquired by it was in October, 1937, in excess of the full claim of the Realty Associates (fols. 354-233-4-228). By elimination, the only creditors were the respondents and therefore there were no creditors who could have been preferred against.

The petitioner's arguments on its second cause of action which also is based upon Section 15 of the Stock Corporation Law are fully refuted in the opinion rendered by the Circuit Court in unanimously affirming the dismissal of the complaint by the District Judge. *Corney*

v. *Salzman*, 22 F. (2) 268; *Prudence Co. Inc.*, 16 F. Supp. 282; New York State Civil Practice Act, Section 1077, Sections A and B; *Emerson* v. *Berman*, 57 Fed. (2) 637.

Conclusion.

The petition for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit should be denied.

Respectfully submitted,

MICHAEL HALPERIN,
Attorney for Respondents,
(Defendants below).